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FM AMEMBASSY BISHKEK
TO RUEHC/SECSTATE WASHDC IMMEDIATE 0184
INFO RUCNCLS/ALL SOUTH AND CENTRAL ASIA COLLECTIVE
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RUEHBJ/AMEMBASSY BEIJING 2276
RUEAUSA/USDA WASHDC
RUEATRS/TREASURY WASHDC
RHEFDIA/DIA WASHDC
RUEKJCS/OSD WASHDC
RUEAIIA/CIA WASHDC
RHEHNSC/NSC WASHDC
RUEKJCS/SECDEF WASHDC
RUEKJCS/JOINT STAFF WASHDC
RUEHGV/USMISSION GENEVA 0709
RUEHVEN/USMISSION USOSCE 2680
RUCNDT/USMISSION USUN NEW YORK 2060
RUEHNO/USMISSION USNATO BRUSSELS BE
RUEHBS/USEU BRUSSELS
RUEHLMC/MILLENNIUM CHALLENGE CORP
RUMICEA/USCENTCOM INTEL CEN MACDILL AFB FL

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SUBJECT: KYRGYZ FEEL INFLATIONARY AND FINANCIAL PRESSURES

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¶1. (SBU) Summary: With "official" monthly food price inflation of 2.3%, hoarding and rapid price inflation are affecting an increasing array of foodstuffs in Kyrgyz markets. Meanwhile, the Kyrgyz Central Bank has pumped the equivalent of over \$150 million into the local currency market to curb Kyrgyz som appreciation against the dollar and protect dollar-denominated savings of many Kyrgyz citizens. Despite the heavy reliance of Kyrgyz banks on Kazakh capital, there has been no observed "pullback" of Kazakh funds from Kyrgyz banks. However, Kyrgyz media report that Kyrgyz banks have begun limiting credit to local applicants. With the upcoming constitutional referendum and the possibility of early parliamentary elections, bread and butter issues will likely play a greater role in political debate in the coming weeks. End summary.

Inflation and Hoarding Affect Food Supplies

¶2. (SBU) Amidst sharply increasing wheat and bread prices, anecdotal reports indicate that cooking oil is becoming scarce throughout the country. A local IMF official told emboff September 20 that Kyrgyz Central Bank-commissioned surveying revealed monthly food price inflation of 2.3%. The IMF official reasoned that recent, significant monetary supply growth (which has been supported by customs levies on a surge in Chinese imports) has finally fueled an inflationary spiral. However, Embassy staff observations as well as press accounts in recent weeks indicate price appreciation above the Central Bank's 2.3% figure.

Pressure on the Dollar

¶3. (SBU) Despite an increased supply of Kyrgyz soms, the

continued inflow of dollar-dominated remittances and increasing concerns about the U.S. dollar have led to a slight appreciation of the Kyrgyz som. (Note: The current exchange rate is 37 soms to the dollar. End note.) According to the IMF official, the Kyrgyz Central Bank has pumped the equivalent of over \$150 million into the local currency market since the spring to moderate the som's appreciation. As many Kyrgyz continue to retain their savings in dollars, and as many large value transactions are made in dollars, the Central Bank has attempted to maintain the value of personal savings in the Kyrgyz Republic. In the short term, the Central Bank appears to have sufficient reserves to continue its interventionist policy.

Impact of Kazakh Credit Crunch

14. (SBU) While some local observers have predicted that the Bishkek real estate price boom will soon collapse, others note that continued demand for new housing stock will sustain real estate price increases. However, concerns that Kazakh banks are restricting credit have sent a shudder through Kyrgyz banking circles. Although the IMF official noted that there has been no "pullback" of Kazakh capital from Kyrgyz banks, he expressed concern about the heavy reliance of Kyrgyz banks on their Kazakh neighbors. A Kazakh financial "burp," he added, would generate severe gastrointestinal distress for Kyrgyz banks. Regardless, Kyrgyz media report that Kyrgyz banks have curtailed their lending activities.

Comment

15. (SBU) Kyrgyz officials have begun to respond to concerns about food prices, supply shortages and possible social discord. With the advent of a constitutional referendum and

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possible parliamentary elections, bread and butter issues may become increasingly prominent in the political debate. While the government's attempts to control bread price inflation have not had the desired effect (supplies are limited, quality is down and loaves have decreased in size), the government may also not be able to stabilize prices for a broader basket of goods. Embassy will continue to monitor market developments.
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